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No. 84

IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1943

Dixie Pine Products Company, Petitioner

vs

Commissioner of Internal Revenue, Respondent

BRIEF FOR THE PETITIONER

T. J. WILLS
Solicitor for Petitioner

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BRIEF FOR THE PETITIONER

MAY IT PLEASE THE COURT:

The petitioner, taxpayer, asserts that the opinion of of the Circuit Court of Appeals of the Fifth Circuit, and the judgment entered thereon, is erroneous and should be reversed.

Petitioner kept its books on an accrual basis. In the year 1937 it accrued $20,839.38 tax assessed and demanded of it by the State of Mississippi. Credit for the tax so accrued was taken against the gross income upon which the income tax was paid.

The Commissioner, respondent, on April 15, 1940, disallowed this accrued deduction and assessed a deficiency tax of $3600.09 and an excess profit tax of $1169.-95. (record page 7).

A hearing was had before the Commissioner and the assessment of the tax was approved by him. An appeal from his decision was prosecuted before the Board of Tax Appeals. The Board of Tax Appeals affirmed the

assessment. The case was then carried to the Circuit Court of Appeals and there affirmed. (record page 46 et sequa).

It is contended by petitioner that the opinion of the Circuit Court of Appeals in this case is in conflict with the cases of **Commissioner of Internal Revenue v. Central United States National Bank, 99 Fed. (2nd) page 568** from the sixth circuit, **J. A. Dougherty & Sons v. The Commissioner, 121 Fed. (2nd) 700** from the third circuit and **Davies Estate v. Commissioner, 126 Fed. (2nd) 294,** from the sixth circuit.

Petitioner accrued the tax and took the deduction under the provisions of section 23 * * (c) of the Revenue Act of 1936. The language of the act is

> "In computing net income there shall be allowed as deductions *** (c) taxes generally—taxes paid or accrued within the taxable year, except—"

Section 23 (a) provides for deductions for the necessary expense incurred in the carrying on of the business, the language of the statute being:

> "In computing net income there shall be allowed as deductions:
>
> (a) Expenses.—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business; and rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which

he has no equity."

The Circuit Court of Appeals of the Fifth circuit, in affirming the assessment of the tax, said:

> "The petitioner contends that its 1937 accrual and deduction of the tax item $20,839.38 was proper, and that the Board of Tax Appeals erred in holding that this amount was not deductible from the gross income of that year. The decision of the Board is without error. During the whole of the tax year for which the right of deduction is asserted, Dixie Pine Products Company was denying liability for the State gasoline tax and was affirmatively litigating the applicability of the taxing statute to the solvent used by it. Indeed when it stopped paying the taxes assessed against it by the Motor Vehicle Commissioner, it had won the first round of litigation in the Supreme Court of Mississippi."

The court then cited in support of its holding the cases

Commissioner v. Southeastern Express Co., 56 Fed. 2nd 600;

Lucas v. American Code Co., 280 U. S. 445;

Brown v. Helvering, 291 U. S. 193;

Pharr & Sons v. Commissioner, 56 Fed. 2nd 832.

Petitioner asserts that these cases correctly interpret deductions allowed under the provisions of section 23 (a) of the Revenue Act in question.

The liability of the taxpayers, in the cases above cited and relied on by the Circuit Court of Appeals, were accruals and deductions against liability growing out of private transactions and subject to private settlements. The cases have no reference whatsoever to a liability imposed by statute or the accrual of a tax.

HISTORY OF THE CASE

Petitioner is engaged in the naval stores business. It extracts rosin from the pine stumps and deadwood left behind the saw mill operations in the yellow pine belt. There were in 1937 five such plants operating in different sections of the State of Mississippi. In an operation of this character a solvent is used to dissolve the rosin from the pine chips that have had the turpentine and pine oil removed by steam. Petitioner used between 300,000 and 400,00 gallons of the solvent annually.

The State of Mississippi in 1932 imposed a gasoline tax of 6c per gallon on all gasoline and petroleum products meeting a certain test that was used, consumed or sold in the State of Mississippi. This reducing agent, or solvent, used by the petitioner was a cut of gasoline having an initial boiling point of 230 degrees fahrenheit and a vanishing point of 290 degrees fahrenheit, whereas gasoline itself had an initial boiling point of 80 degrees fahrenheit and a vanishing point of 432 degrees fahrenheit.

The naval stores plants using this solvent did not pay the gasolne tax imposed by Legislature enactment for the four years from 1932 to 1936.

In 1936 the Legislature appointed a Roving Committee to make investigations of businesses in the State that had escaped paying gasoline tax. This Roving Committee demanded the tax of five naval stores plants and finally adjusted it with them for 1-4 of 1% per gallon in lieu of the 6c levied by the statute.

The Legislature in 1936 amended the gasoline revenue law. It created the office of Commissioner of Motor Vehicles, with powers and authority to levy and collect all gasoline taxes. The effective date of the act was May 1st, 1936.

The Roving Committee, in its many searches and meanderings about the state, did not make demand for this tax until July, 1936. An adjustment was made about August 1st. The 1936 Act, however, had become effective as of May 1st and the Commissioner had no authority to waive any part of the tax. He was required to collect the tax plus a 25% penalty for delinquency.

The five naval stores companies, including petitioner herein, began paying the tax on September 1, 1936. They left the tax that had accrued, with the penalty thereon, from May 1st to September 1st, open for future negotiations and final adjustment.

This petitioner thereupon filed a bill in the Chancery Court of Hinds County, asking for an injunction restraining the Commissioner from collecting the tax. The suit was one that might be called a friendly or collusive. What is meant by it being a collusive suit is that the petitioner and the Motor Vehicle Commissioner, through their attorneys, drew a bill setting forth all of the facts as contended for by both parties. The Motor Vehicle Commissioner agreed to interpose a demurrer thereto. A decision on the demurrer would determine the liability of the complainant for the tax.

The bill of complaint was filed. A demurrer was interposed and the Chancellor sustained the demurrer and dismissed the bill. An appeal was prosecuted to the State Supreme Court and was there reversed.

The decision of the Supreme Court was handed down on January 25th, 1937. The Supreme Court held that under the statement of facts set forth in the bill of complaint that the gasoline tax did not apply to the solvent. Of course, the decision being from a decree sustaining a demurrer, the case was remanded for further proceedings in accordance with the opinion rendered. Appellant immediately ceased to pay the tax for the rea-

son that the facts set forth in the bill of complaint represented the facts as agreed on by the Motor Vehicle Commissioner and the taxpayer, petitioner here.

In presenting the case to the Supreme Court it was urged that to hold that the tax applied would strike down the statute.

The bill of complaint filed in the Chancery Court, asking for the injunction, stated all of the facts, enumerating the properties of the solvent. These facts brought the solvent clearly within the definition of the statute levying the tax. In seeking, however, a favorable decision, the petition alleged that the solvent was not gasoline within the definition of gasoline. Section 5 (a) Chapter 162 Acts of 1936. It alleged that it was not used or usable in propelling motor vehicles when used alone, and was not a liquid that is ordinarily or practically commercially usable in internal combustion engines for the generation of power. It reiterated, however, that the solvent is a petroleum product and has a gravity test above 46 degrees T.B. scale at a temperature of 60 degrees fahrenheit, and that it could be mixed or blended with other petroleum products so as to make it usable as a motor vehicle fuel.

The petition filed, charged that the solvent was not gasoline and then admitted that it contained all the properties and characteristics necessary to meet the requirements of the definition of gasoline in the act. This was done for the purpose of obtaining a judicial interpretation of the act that would square it with the constitution of the United States and of the State. Such an interpretation would change the definition of gasoline by judicial Legislation by giving it that meaning that would not strike the act down.

The opinion in the case held that the bill of complaint was good as against a demurrer. **Dixie Pine Products Company v. Dyer, 178 Miss. 227, 172 Sou. 145.**

This decision of the Court, under the agreement had with the Attorney General, that the bill of complaint stated all the facts would settle the law of the case. The taxpayer then ceased paying the state tax.

In May of 1937, however, the Motor Vehicle Commissioner, filed an answer in the cause denying every fact set forth in the bill of complaint, upon which the Supreme Court had based its decision. The other four industries continued to pay the tax. Petitioner herein, under advice of counsel, declined to pay the tax but being on an accrual basis, accrued it. There was no provision for a refund of the tax, if erroneously paid in, and for that reason the petitioner here was advised not to pay the tax in but to accrue it and await the final outcome of the case.

If the facts, as stated by the Motor Vehicle Commissioner, in his answer were to be established, then the tax would apply unless the contention of the taxpayer, that to so interpret the statute would strike it down, as being in conflict with the constitution should prevail.

The taxpayer had not paid the tax from the first of the year 1937 up until June 1, 1939, and all the penalties provided by statute for non payment of the tax had accrued before the answer was filed. The taxpayer accrued the tax but did not pay it. The reason for not paying it was that there was no provision for a refund of a tax erroneously paid.

In December 1938 a stipulation was made and filed in the case pending, stipulating the facts, the same as they were in the bill of complaint. This stipulation of facts then made the former opinion of the Supreme Court the law of the case and there was no possible chance for a different holding or a contrary decree being entered.

The Chancellor, in December of 1938, entered a final decree enjoining the collection of the tax holding that it

did not apply to the solvent. Petitioner herein, thereupon took into its accounts, as a re-captured profit, the sum of $20,839.83, which had been accrued and held against the tax liability.

ARGUMENT

The true rule of law, with reference to the accruals and credits of a tax assessed, was stated in the case o **Central United National Bank. 99 Fed. (2nd) page 568.** The court in effect said that since the tax had been assessed and it would require a court decision to relieve the taxpayer of the payment, that it is proper to accrue the tax and to deduct it from the gross income for the year in which it is accrued.

In the case of **Dougherty & Sons v. Commissioner of Internal Revenue, 121 Fed. (2nd) page 700,** the court held that where a taxpayer's books are kept on an accrual basis that the taxpayer is entitled to deduct from the gross income tax set up on its books, within the taxable year, the tax so accrued under the statute, even though subsequently it is held unconstitutional and the tax is never paid.

In the case of **Davies Estate v. Commissioner, 126 Fed. (2nd) 294,** the court cited with approval the Dougherty case, holding that the taxpayer had a right to accrue and deduct a tax so assessed against it in the year of the accrual. The court cited the case of **Chicot County Drainage District v. Baxter State Bank, 308 U. S. 371, 60 Sup. Ct. Rep. page 317,** where the court said:

> "The actual existence of a statute prior to determination of its unconstitutionality is an operative fact and may have consequences which cannot be justly ignored."

The statute of the State of Mississippi was plain and unambiguous. The solvent came within the terms of the

definition of gasoline. To so apply the statute, however, would strike it down or render it so impotent, under the authority of **Bingaman v. Golden Eagle Western Lines 297, U. S. 626, 56 Sup. Ct. Rept. 624,** that it would destroy the entire highway scheme of the state. What the court would do with the case on the bill of complaint and answer of the Commissioner, and proof thereunder, was less predictable than would be the holding of the unconstitutionality of a statute. The accrual of the tax was proper. The taking of the deduction from the gross income for the year in which the tax was accrued was proper.

The decision of the Circuit Court of the Fifth Circuit, in this case, brought it in conflict with the cases of **Central United National Bank, 99 Fed. (2nd) 568. Dougherty & Sons v. Commissioner, 121 Fed. (2nd) 700 and Davies Estate v. Commissioner, 126 Fed. (2nd) 294.**

The cases relied on by the Circuit Court of Appeals were not in point in that they were interpreting section 23 (a) of the Revenue Act whereas this case as the Bank case, the Dougherty case and the Davies case is controlled by section (c) of the Revenue Act.

The decision of the Fifth Circuit Court, being in conflict, should be reversed.

Respectfully submitted,

T. J. WILLS

Solicitor for Petitioner

APPENDIX

Chapter 162 Laws of 1936

DEFINITIONS.

Sec. 5 (a) The word "gasoline" as used in this act shall include all liquid fuels which are used or usable in propelling motor vehicles, either when used alone or when mixed, blended, or compounded, including liquids ordinarily, practically and commercially, usable in internal combustion engines for the generation of power, and all distillates of, and condensates from petroleum, natural gas, coal, coal tar, vegetable ferments, and other products so usable and received in this state, having a gravity test above 46 degrees tagliaubes baume scale, at temperature of 60 degrees F.

EXCISE TAX ON GASOLINE AND OIL.

Sec. 8. Any person engaged in business as a distributor, as defined in this act, shall pay for the privilege of engaging in such business an excise tax equal to and computed as follows:

(a) Six cents (6c) per gallon on all gasoline stored, sold, distributed, manufactured, refined, distilled, blended or compounded in this state or received in this state for sale, use on the highways, storage, distribution, use in internal combustion engines, or for any commercial purposes.

PURPOSE OF ACT.
Sec. 35.

For the purpose of this act it will be prima facie presumed that all gasoline and oil, or either, as defined herein, imported, received, purchased, acquired, used, stored,

manufactured, refined, distilled, blended, compounded, sold or distributed in this state is intended for use in propelling motor vehicles on the public roads and highways, and the tax liability in this act is based on such presumption. It is the further purpose of this act to provide for the refunding to the consumer of all tax actually paid, less one cent (1c) per gallon, on gasoline not used in propelling motor vehicles on the public highways and roads. All gasoline and oil, or either, entering the State of Mississippi shall be used in computing the tax, except gasoline and oil, or either, brought into the state in the reservoir provided by the manufacturer as the container for motor fuel used in propelling said motor vehicle, not to exceed twenty (20) gallons.